IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF TEXAS
SHERMAN DIVISION

IN RE:	§	
	§	
DIANE M. DAVIS,	§	Case No. 09-42865
	§	(Chapter 13)
Debtor.	§	

MEMORANDUM OPINION

On March 31, 2011, this Court entered a Memorandum Opinion and Order regarding the debtor's objections to several unsecured credit card claims filed in her bankruptcy case. The Order, among other things, required counsel for the debtor to appear and show cause why the Court should not impose sanctions upon him. The Court conducted a show cause hearing on May 12, 2011. The following constitutes the Court's findings of fact and conclusions of law.

I. Jurisdiction

The Court has subject matter jurisdiction over this bankruptcy case pursuant to 28 U.S.C. § 1334(a). This is a core proceeding under 28 U.S.C. §§ 157(b)(2)(A) and (O). The Court retains jurisdiction over this matter even though the Court granted the debtor's motion to dismiss her case on September 6, 2011. *See Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384, 395 (1990).

II. Background

The Court detailed the facts leading up to the show cause hearing in its March 31st Memorandum Opinion. In summary, counsel is an experienced bankruptcy attorney. His client was an affluent single woman who filed for bankruptcy solely to address her credit card debt. Although the debtor filed a petition for relief under chapter 13, and she

stated in her reorganization plan that all of her creditors would be paid in full, she did not, in fact, intend to repay any of her credit card debts.

In hindsight, the debtor's true intent is clear from her conduct in this case, starting with her bankruptcy schedules.[1] The debtor listed all of her $150,360 in credit card debt as disputed in her "Schedule F – Creditors Holding Unsecured Nonpriority Claims." She stated in her Schedule F that she was listing the balance shown on the last statement she had received from each creditor, but that she was "not presently able to determine if [the] balance is correct" or whether "trade name is correct legal creditor [sic]." Despite this protestation, the debtor and her counsel were certain enough of the creditors' names and addresses to use the information in the debtor's Schedule F to notify creditors of the debtor's bankruptcy case and the deadline for filing proofs of claim.[2]

The debtor submitted a plan in which she proposed to repay all of her creditors in full. Most of the debtor's unsecured creditors filed timely claims in her case. Her plan, not surprisingly, drew no objections from them. As modified by Congress in 2005, the Code requires an accelerated confirmation process. The Court, therefore, confirmed the debtor's proposed plan subject to the claims allowance process.

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[1] The Code requires a debtor to disclose all assets and liabilities by completing the Form 6 Schedules (Schedules A – J). *See* 11 U.S.C. § 521(1). The Bankruptcy Rules require the debtor to verify the Form 6 Schedules under oath, *see* FED. R. BANKR. P. 1008, and bankruptcy courts rely on the accuracy of the schedules in determining, for example, whether a debtor is eligible for chapter 13 or whether to confirm a proposed plan of reorganization.

[2] The bankruptcy clerk must mail creditors notice of the deadline for filing proofs of claim. *See* FED. R. BANKR. P. 2002(a)(7). The Code requires a debtor to file a list of her creditors, including their addresses, so that the clerk may meet this obligation. . 11 U.S.C. § 521(1)(a). In addition, this Court's local rules require that debtors file a mailing matrix to assist in the process of giving notice. *See* Local Bankruptcy Rule ("LBR") 1007.

Several months after obtaining confirmation of her plan, the debtor objected to all of the claims for credit card debt filed in her case.[3] The debtor's objections were substantially identical. Although a failure to attach documents to the proof of claim form (Official Form 10) is not listed as a grounds for disallowance of a claim under § 502(b) of the Code, her objection to each of the claims for credit card debt was that the claimants allegedly failed to attach sufficient documentation to their proofs of claim. The debtor submitted affidavits in support of the objections in which she stated that, looking solely at the proofs of claim, she could not tell whether she owed the claimants any debts. The claimants discussed in the March 31st Memorandum Opinion did not request an evidentiary hearing by responding.

Although the Court could have ruled on the papers, the Court scheduled a hearing on the debtor's objections in order to allow the debtor an opportunity to satisfy her burden of proof. Bankruptcy courts, including this one, generally require a party who is objecting to a claim to produce evidence which is at least equal in probative force to that offered by proof of claim, and which, if believed, would refute at least one of allegations essential to the claim's legal sufficiency. *See, e.g., In re Rally Partners, L.P.*, 306 B.R. 165, 168-169 (Bankr. E.D. Tex. 2003)). At the hearing, the Court pointed out that the debtor's objections failed to satisfy this burden inasmuch as her affidavits did not clearly deny her liability to the claimants or raise any other substantive objection to their proofs of claim. Because counsel was unprepared to address the Court's concerns, the Court

[3] The Code allows a party-in-interest to object to a claim by asserting one of the grounds for disallowance set forth in § 502(b).[3] If a party objects, "the court, after notice and a hearing, shall determine the amount of such claim." 11 U.S.C. § 502(b). The Code defines the phrase "after notice and a hearing" to "authorize[ ] an act without an actual hearing if such notice is given properly and if ... such a hearing is not requested timely by a party in interest." *Id.* at § 102(1)(B)(i). The Local Bankruptcy Rules require a debtor to include "negative notice," that is, notice that the Court may grant the objection as unopposed is no response is timely filed. *See* LBR 9007(a).

continued the hearing. At counsel's request, the Court continued the hearing a second time so that the debtor could attend. The debtor was present at the final hearing, but counsel declined to offer any testimony from her or other evidence in support of her claim objections. Following the conclusion of the hearing, the Court overruled the debtor's objections for the reasons stated in the Memorandum Opinion.

In the Memorandum Opinion, the Court questioned whether counsel conducted any factual investigation prior to filing the debtor's Schedule F. The Court also questioned whether counsel deliberately misled creditors by filing a proposed plan in which the debtor stated that she intended to repay all of her unsecured creditors in full when, in fact, the debtor intended to dispute any claim they might file. Further, it appeared that counsel may have deliberately ignored his client's personal knowledge in crafting affidavits in support of her claim objections. The debtor admitted in her Schedule F that she reviewed the last statements she had received relating to her credit card debts in order to prepare her schedules, and she admitted in her Statement of Financial Affairs that she had made payments to several of these creditors in the months prior to bankruptcy. Nonetheless, counsel for the debtor prepared affidavits in which the debtor denied that she owed any debt to the claimants because, *based solely on the documentation attached to the proofs of claim*, she could not determine her liability.

At the show cause hearing, counsel testified that he was not entirely sure the debtor had provided him with the correct names and addresses for the creditors holding her credit card debts. Counsel testified that his client had not kept copies of the underlying credit card agreements and that the information he received from his client did not exactly match the claims for credit card debt eventually filed in her case. Since these

claimants did not attach what counsel believed to be all of the legally required documentation to their proofs of claim, he recommended that the debtor object to all of their claims. The debtor accepted his advice and signed the affidavits he prepared.

III. Discussion

The debtor filed for bankruptcy in order to discharge more than $150,000 in credit card debts. Although she obtained confirmation of a chapter 13 plan in which she stated that she would receive a discharge after repaying her creditors in full, she attempted to use the claims allowance process to achieve the functional equivalent of a chapter 7 discharge. Counsel filed bankruptcy schedules in which the debtor disputed the entirety of every single credit card debt, and he filed substantially identical objections to all of the claims relating to the debtor's credit card debts. The objections and supporting affidavits appeared to artfully avoid addressing the debtor's personal knowledge of her debts. This Court provided the debtor with an opportunity to supplement her affidavits by, for example, testifying that she did not owe a debt to the claimants. Despite several continuances of that hearing in order to accommodate the debtor's schedule, counsel for the debtor chose to produce no testimony from his client.

A.

The Court scheduled a show cause hearing in order to determine whether counsel's conduct violated Bankruptcy Rule 9011(b) and, if so, whether to sanction him. *See* FED. R. BANKR. P. 9011(b).[4] Rule 9011(b) provides that an attorney who presents "a petition, pleading, written motion, or other paper" to the court, whether by "signing, filing, submitting, or later advocating," makes four certifications to the court. FED. R.

[4] Rule 9011 is substantially identical to Federal Rule of Civil Procedure 11 and, therefore, courts may refer to Rule 11 jurisprudence when considering sanctions under Rule 9011. *See In re Pratt*, 524 F.3d 580, 585 (5th Cir. 2008).

BANKR. P. 9011(b). Three are certifications that the legal assertions in the case have a basis in the law (or a fair argument for the law's modification), and the factual contentions and denials in the case have evidentiary support or are likely to after a reasonable opportunity for investigation. FED. R. BANKR. P. 9011(b)(2)-(4). The fourth is a certification that the paper "is not being presented for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation." FED. R. BANKR. P. 9011(b)(1).

Here, as outlined in the Court's March 31st Memorandum Opinion, it appeared that counsel had participated in or facilitated a scheme to improperly manipulate the bankruptcy process. The scheme appeared to begin with a Schedule F in which the debtor fabricated a dispute as to all of her credit card debts. After obtaining confirmation of a chapter 13 plan to repay creditors in full, counsel sought to obtain orders completely disallowing each and every one of the credit card claims. In a brief in support of the debtor's objections, counsel argued that the Court should disallow the claims based on the creditors' alleged noncompliance with Bankruptcy Rule 3001 and Official Form 10. His arguments essentially raised a lack of documentation objection, but he conveniently ignored the billing statements the debtor admitted having in her possession when she filled out her schedules.

At the show cause hearing, counsel testified that he objected to all of the credit card claims in the debtor's case based on his review of the proofs of claim. He argued that lack of documentation is a substantive objection to a claim under § 502(b)(1) and that he is not required to do any research prior to filing a claim objection other than looking at the proof of claim. This is not the issue he presented for the Court to decide at

the hearing on the debtor's claim objections. If counsel had simply asserted an objection based on lack of documentation, the Court could have disposed of the matter quickly. The Court has ruled on many occasions that lack of documentation, without more, is not grounds to disallow a claim under § 502(b)(1) of the Code.

This case was not so clear-cut. Counsel did not simply file an objection to a claim asserting lack of documentation as grounds for disallowance. He filed a Schedule F in which he listed the entirety of all of the debtor's credit card debts as disputed, and he filed objections to every unsecured claim – all for credit card debts – exceeding a total of $150,000. If he honestly believed the debtor's creditors could not collect their debts under Texas law, his client had no genuine need for bankruptcy protection. It appeared to the Court he was arguing positions he knew to be false. He put forward no evidence that the debtor had substantive objections arising under Texas law that would put the entirety of any of the claims in dispute. Indeed, he withdrew substantially all of the objections when the creditors responded.

Counsel's conduct drew the Court's attention because he violated the principle of too much. As the Fifth Circuit explained in the context of pre-bankruptcy planning, "phrased colloquially, when a pig becomes a hog it is slaughtered." *See Matter of Swift*, 3 F.3d 929, 931 (5th Cir. 1993). Counsel participated in a scheme wherein the debtor became a hog. Although he filed a plan stating that the debtor would repay her creditors in full over time, he attempted to use the claims allowance process to achieve a quick discharge of her credit card debts without paying creditors a single penny. His use of substantially identical objections and affidavits further supports the conclusion that he

conducted no reasonable pre-filing investigation. *See Terran v. Kaplan*, 109 F.3d 1428, 1434-35 (9th Cir. 1997).

When an attorney facilitates the filing of schedules that contain false or manufactured disputes, when he files a plan that falsely states creditors will be paid in full, and when he then misuses the claims allowance process by filing lack of documentation objections to claims while having documentation in hand, all in a scheme to obtain the functional equivalent of a chapter 7 discharge, the attorney violates Bankruptcy Rule 9011. Moreover, with respect to the objections to claims, counsel failed in his duty under Bankruptcy Rule 9011 to make a reasonable inquiry into the facts and law before filing the schedules and presenting objections to the Court. It is clearly not permissible to file claims objections and then wait and see how the claimants respond as the sole means of finding out whether you have a dispute.

B.

This Court may act *sua sponte* in imposing sanctions under the Bankruptcy Rules. *See Chambers v. Nasco*, 501 U.S. 32, 42 n.8 (1991). When the Court initiates a Bankruptcy Rule 9011 proceeding, Bankruptcy Rule 9011(c)(2) limits the available monetary sanction to "an order to pay a penalty into court." FED. R. BANKR. P. 9011(c)(2). Generally, a court enjoys broad discretion in determining the appropriate size of that penalty, *see Thomas v. Capital Security Servs., Inc.*, 836 F.2d 866, 877 (5th Cir. 1988) (en banc), provided it is no greater than "what is sufficient to deter repetition of such conduct or comparable conduct by others similarly situated," FED. R. BANKR.P. 9011(c)(2).

It would probably not take much of a monetary sanction to deter counsel. He has been put to the trouble and expense of hiring an attorney and appearing at a sanctions hearing, and he has suffered the embarrassment of having a public hearing regarding whether he acted improperly and a finding that he, in fact, committed the committed improper acts. This Court recognizes that counsel is a competent and zealous advocate for his clients, but in this case he went too far. As this case demonstrates, "'bankruptcy proceedings are subject to a degree of manipulation and abuse not typical of civil litigation.'" *In re Collins*, 250 B.R. 645, 660 (Bankr. N.D. Ill. 2000) (quoting *Marsch v. Marsch (In re Marsch),* 36 F.3d 825, 830 (9th Cir. 1994)). Accordingly, for his violations of Bankruptcy Rule 9011(b)(1) and (3), the Court will order counsel to pay a penalty of $500.00.

IV. Conclusion

For these reasons, the Court finds that counsel engaged in an improper scheme to avoid the ramifications of § 707(b)(1) on the ability of affluent debtors to obtain a quick discharge of their unsecured debts. The Court further finds that counsel filed a Schedule F and objections to claims without regard to information in his or the debtor's possession, without conducting any factual investigation, and for an improper purpose in violation of Bankruptcy Rule 9011(b). Pursuant to Bankruptcy Rule 9011(c)(2), counsel is ordered to pay to the Clerk of the Bankruptcy Court a penalty of $500.00. Payment is due in 30 days. A separate order will be entered consistent with this opinion.

Signed on 9/30/2011

Brenda T. Rhoades MD

HONORABLE BRENDA T. RHOADES,
CHIEF UNITED STATES BANKRUPTCY JUDGE